



5001-06-P

**DEPARTMENT OF DEFENSE**

**Defense Acquisition Regulations System**

**48 CFR Parts 204, 232, and 252**

**[Docket DARS-2019-0019]**

**RIN 0750-AK37**

**Performance-Based Payments (DFARS Case 2019-D002)**

**AGENCY:** Defense Acquisition Regulations System, Department of Defense (DoD).

**ACTION:** Proposed rule.

**SUMMARY:** DoD is proposing to amend the Defense Federal Acquisition Regulation Supplement (DFARS) to implement a section of the National Defense Authorization Act for Fiscal Year 2017, which amends 10 U.S.C. 2307 to address the use of performance-based payments.

**DATES:** *Comment Date:* Comments on the proposed rule should be submitted in writing to the address shown below on or before

**[Insert date 60 days after date of publication in the FEDERAL REGISTER]**, to be considered in the formation of a final rule.

**ADDRESSES:** *Submission of Comments:* Submit comments identified by DFARS Case 2019-D002, using any of the following methods:

- o *Federal eRulemaking Portal:* <http://www.regulations.gov>. Search for "DFARS Case 2019-D002." Select "Comment Now" and follow the instructions provided to submit a comment. Please

include "DFARS Case 2019-D002" on any attached documents.

- o *Email:* *osd.dfars@mail.mil.* Include DFARS Case 2019-D002 in the subject line of the message.

- o *Fax:* 571-372-6094.

- o *Mail:* Defense Acquisition Regulations System, Attn: Ms. Amy G. Williams, OUSD(A&S)DPC/DARS, Room 3B941, 3060 Defense Pentagon, Washington, DC 20301-3060.

Comments received generally will be posted without change to <http://www.regulations.gov>, including any personal information provided. To confirm receipt of your comment(s), please check [www.regulations.gov](http://www.regulations.gov), approximately two to three days after submission to verify posting (except allow 30 days for posting of comments submitted by mail).

**FOR FURTHER INFORMATION CONTACT:** Ms. Amy Williams, DPC/DARS, at 571-372-6106.

**SUPPLEMENTARY INFORMATION:**

**I. Background**

DoD is proposing to amend DFARS subpart 232.10, Performance-Based Payments; amend the clauses at DFARS 252.232-7012, Performance-Based Payments—Whole Contract Basis, and DFARS 252.232-7013, Performance-Based Payments—Deliverable Item Basis; and add a new provision at 252.232-70XX, Performance-Based Payments—Representation, to implement section 831 the National Defense Authorization Act (NDAA) for Fiscal Year (FY) 2017,

which amends 10 U.S.C. 2307 to address the use of performance-based payments.

A proposed rule was published in the *Federal Register* on August 23, 2018 (83 FR 42831), under DFARS Case 2017-D019, Performance-Based Payments and Progress Payments. That rule proposed to implement section 831 and also revise progress payments and performance-based payments policies and procedures for DoD contracts. That proposed rule was withdrawn by a notice published in the *Federal Register* on October 4, 2018 (83 FR 47867). This rule addresses only the amendments to the DFARS required by section 831.

## **II. Discussion and Analysis**

### *A. Preference for performance-based payments.*

Performance-based payments are a method of contract financing that may be available under fixed-price contracts, except for contracts awarded using Sealed Bidding procedures. Performance-based payments differ from the more traditional progress payments based on costs because these contract financing payments are made on the basis of the contractor's achievement of objective, quantifiably measurable events, results, or accomplishments that are defined and valued in the contract prior to performance. It is a preferred method of contracting as it may reduce oversight and compliance costs to the Government. It also has benefits for contractors as it should

help cash flow, reduce the cost of oversight and compliance, and allows the management team to focus on technical and schedule progress.

Section 831 amends 10 U.S.C. 2307(b)(1) by requiring, whenever practicable, that payment under the authority of 10 U.S.C. 2307(a) shall be made using performance-based payments. Federal Acquisition Regulation (FAR) 32.1001(a) already states that performance-based payments are the preferred Government financing method when the contracting officer finds them practical, and the contractor agrees to their use.

*B. Relationship of performance-based payments to costs incurred.*

DFARS case 2011-D045, published in the *Federal Register* on March 31, 2014 (77 FR 4638), mandated that cumulative performance-based payments shall not exceed the cumulative cost incurred on the contract or delivery item, whichever is applicable, at any point during contract performance. That requirement was supported by the statement at FAR 32.1004(b)(2)(i) that contract financing should only be provided to the extent actually needed for contract performance and the statement at FAR 32.1004(b)(3)(ii) that the contracting officer must ensure that performance-based payments "are not expected to result in an unreasonably low or negative level of contractor investment in the contract."

Section 831 amended 10 U.S.C. 2307 by adding paragraph (b) (2), which provides that performance-based payments shall not be conditioned upon costs incurred in contract performance but only on the achievement of negotiated performance outcomes.

Therefore, this rule proposes to remove the restrictions at DFARS 232.1001(a) and paragraph (b) (i) of the clauses at DFARS 252.232-7012 and 252.232-7013 that limit performance-based payments to amounts not greater than costs incurred up to the time of payment. However, the requirement for contractors to report costs incurred when requesting performance-based payments is retained, in order to have the data necessary for negotiation of performance-based payments on future contracts.

Section 831 also added paragraph (b) (3) to 10 U.S.C. 2307, which addresses the eligibility for performance-based payments of nontraditional defense contractors and other private sector companies. This has been added to the policy at DFARS 232.1001.

10 U.S.C. 2307(b) (4), as added by section 831, requires contractors to be in compliance with Generally Accepted Accounting Principles in order to receive performance-based payments, with no requirement for a Government-unique accounting systems or practices as a prerequisite to receive performance-based payments. This requirement has been incorporated at DFARS 232.1003-70 and the clauses at DFARS 252.232-7012 and 252.232-7013. This rule also proposes a new representation by each

offeror, if performance-based payments are anticipated, as to whether the output of its accounting system is in compliance with Generally Accepted Accounting Principles, as evidenced by audited financial statements.

### **III. Applicability to Contracts at or Below the Simplified Acquisition Threshold and for Commercial Items, Including Commercially Available Off-the-Shelf Items**

This rule proposes to amend the clauses at DFARS 252.232-7012 and 252.232-7013. These clauses do not apply to contracts at or below the simplified acquisition threshold or for the acquisition of commercial items. In accordance with 10 U.S.C. 2307(f) and 41 U.S.C. 4505, FAR 32.201 provides that payment for commercial items may be made under such terms and conditions as the agency head determines are appropriate or customary in the commercial marketplace and are in the best interest of the United States. Furthermore, FAR 32.202-1 states that Government financing of commercial purchases is expected to be different from that used for noncommercial purchases. While the contracting officer may adapt techniques and procedures from the noncommercial subparts for use in implementing commercial contract financing arrangements, the contracting officer must have a full understanding of effects of the differing contract environments and of what is needed to protect the interests of the Government in commercial contract financing.

#### **IV. Expected Cost Impact**

This rule proposes to amend the DFARS to implement changes to performance-based payment policies for DoD contracts by amending the policy on performance-based payments at DFARS 232.1001 and amending the clauses at DFARS 252.232-7012, Performance-Based Payments—Whole Contract Basis, and 252.232-7013, Performance-Based Payments—Deliverable Item Basis.

This rule may benefit contractors who receive contract financing from the Government in the form of performance-based payments. Performance-based payments do not apply to—

- Payments under cost-reimbursement line-items;
- Contracts awarded under the authority of FAR part 12 or part 13;
- Contracts for architect-engineer services or construction, or for shipbuilding or ship repair, when the contract provides for progress payments based upon a percentage or stage of completion.

Performance-based payments are tied to the achievement of specific, measurable events or accomplishments that are defined and valued in advance by the parties to the contract. Total performance-based payments cannot exceed 90 percent of the contract price.

This rulemaking proposes to remove the DFARS restrictions that limit performance-based payments to amounts not greater than costs incurred up to the time of payment.

If performance-based payments to the contractor based on the negotiated value of completed milestone events are allowed to exceed the total costs incurred up to the time of payment, the cost to the contractor of short-term borrowing will decrease and the cost to the Government of borrowing will increase.

In addition, there is a minimal cost to offerors and the Government related to a new provision at DFARS 252.232-70XX, Performance-Based Payments-Representation, that requires each offeror responding to a solicitation that may result in a contract providing performance-based financing to represent whether the output of the offeror's accounting system is in compliance with Generally Accepted Accounting Principles, as evidenced by audited financial statements.

DoD has performed a regulatory cost analysis on this rule. The following is a summary of the estimated public cost savings and Government costs in millions calculated in perpetuity in 2016 dollars at a 7-percent discount rate:

<b>SUMMARY</b>	<b>Public</b>	<b>Government</b>	<b>Total</b>
Present Value	-\$53.971	\$27.338	-\$26.633
Annualized Costs	-\$3.778	\$1.914	-\$1.864
Annualized Value Costs (as of 2016 if Year 1 is 2019)	-\$3.084	\$1.562	-\$1.522



To access the complete Regulatory Cost Analysis, go to the Federal eRulemaking Portal at *www.regulations.gov*, search for "DFARS Case 2019-D002," click "Open Docket," and view "Supporting Documents."

#### **V. Executive Orders 12866 and 13563**

Executive Orders (E.O.s) 12866 and 13563 direct agencies to assess all costs and benefits of available regulatory alternatives and, if regulation is necessary, to select regulatory approaches that maximize net benefits (including potential economic, environmental, public health and safety effects, distributive impacts, and equity). E.O. 13563 emphasizes the importance of quantifying both costs and benefits, of reducing costs, of harmonizing rules, and of promoting flexibility. This is a significant regulatory action and, therefore, was subject to review under section 6(b) of E.O. 12866, Regulatory Planning and Review, dated September 30, 1993. This rule is not a major rule under 5 U.S.C. 804.

#### **VI. Executive Order 13771**

This rule is expected to be an E.O. 13771, Reducing Regulation and Controlling Regulatory Costs, deregulatory action. The total annualized value of the cost savings is \$1,521,836. Details on the estimated cost savings can be found in section IV. of this preamble.

## **VII. Regulatory Flexibility Act**

DoD expects that this proposed rule may have a significant economic impact on a substantial number of small entities within the meaning of the Regulatory Flexibility Act, 5 U.S.C. 601 et seq. Therefore, an initial regulatory flexibility analysis has been prepared and is summarized as follows:

This rule proposes to implement section 831 the National Defense Authorization Act (NDAA) for Fiscal Year (FY) 2017, which amends 10 U.S.C. 2307 to address the use of performance-based payments.

The primary objective of this rule is to remove the restrictions at DFARS 232.1001(a) and the clauses at 252.232-7012(b)(i) and 252.232-7013(b)(i) that limit performance-based payments to amounts not greater than costs incurred up to the time of payment, as required 10 U.S.C. 2307.

This rule will apply to approximately 50 small entities per year that submit offers and are awarded contracts that provide performance-based contract payments from DoD, as well as an additional 5 offerors that submit offers in response to solicitations that may result in contracts that provide performance-based payments but do not receive an award.

This rule adds a reporting requirement that will require an entry in the annual representations and certifications with regard to whether the output of the offeror's accounting system

is in compliance with Generally Accepted Accounting Principles, as evidenced by audited financial statements. DoD estimates that the skill necessary for this requirement is at the journeyman level and that each entry will require an average of 6 minutes.

The rule does not duplicate, overlap, or conflict with any other Federal rules.

This rule will not have a significant economic impact on small entities. The burden imposed by the new representation is minimal. The net impact is likely to benefit small entities, to the extent that the entity may receive an increase in cash flow if the negotiated value of performance-based payment events exceeds the actual costs incurred at the time of event completion. There are no significant alternatives consistent with the stated objectives of the statute.

DoD invites comments from small business concerns and other interested parties on the expected impact of this rule on small entities.

DoD will also consider comments from small entities concerning the existing regulations in subparts affected by this rule in accordance with 5 U.S.C. 610. Interested parties must submit such comments separately and should cite 5 U.S.C. 610 (DFARS Case 2018-D043), in correspondence.

### **XIII. Paperwork Reduction Act**

This rule affects the information collection requirements at DFARS subpart 232.10 (and associated clauses at DFARS 252.232-7012 and 252.232-7013, currently approved under OMB Control Number 0704-0359, DFARS Part 232, Contract Financing. The impact, however, is negligible, because only the last three lines of the table are deleted, which do not impose the predominance of the burden. This rule also adds a new information collection requirement that requires the approval of the Office of Management and Budget under the Paperwork Reduction Act (44 U.S.C. chapter 35). Accordingly, DoD has submitted a request for approval of a new information collection requirement concerning the provision at 252.232-70XX, Performance-Based Payments—Representation to the Office of Management and Budget.

A. Public reporting burden for this collection of information is estimated to average 0.1 hours per response, including the time for reviewing instructions, searching existing data sources, gathering and maintaining the data needed, and completing and reviewing the collection of information.

The annual reporting burden estimated as follows:

Respondents: 144.

Responses per respondent: 1.

Total annual responses: 144.

Preparation hours per response: 0.1 hours

Total response Burden Hours: 14.4.

B. Request for Comments Regarding Paperwork Burden.

Written comments and recommendations on the proposed information collection, including suggestions for reducing this burden, should be sent to Ms. Jasmeet Seehra at the Office of Management and Budget, Desk Officer for DoD, Room 10236, New Executive Office Building, Washington, DC 20503, or e-mail [Jasmeet\\_K.\\_Seehra@omb.eop.gov](mailto:Jasmeet_K._Seehra@omb.eop.gov), with a copy to the Defense Acquisition Regulations System, Attn: Ms. Amy G. Williams, OUSD(A&S)DPC/DARS, Room 3B941, 3060 Defense Pentagon, Washington, DC 20301-3060. Comments can be received from 30 to 60 days after the date of this notice, but comments to OMB will be most useful if received by OMB within 30 days after the date of this notice.

Public comments are particularly invited on: whether this collection of information is necessary for the proper performance of functions of the DFARS, and will have practical utility; whether our estimate of the public burden of this collection of information is accurate, and based on valid assumptions and methodology; ways to enhance the quality, utility, and clarity of the information to be collected; and ways in which we can minimize the burden of the collection of information on those who are to respond, through the use of

appropriate technological collection techniques or other forms of information technology.

To request more information on this proposed information collection or to obtain a copy of the proposal and associated collection instruments, please write to the Defense Acquisition Regulations System, Attn: Ms. Amy G. Williams, OUSD(A&S)DPC/DARS, Room 3B941, 3060 Defense Pentagon, Washington, DC 20301-3060, or email [osd.dfars@mail.mil](mailto:osd.dfars@mail.mil). Include DFARS Case 2019-D002 in the subject line of the message.

**List of Subjects in 48 CFR Parts 204, 232, and 252**

Government procurement.

**Jennifer Lee Hawes,**

*Regulatory Control Officer, Defense Acquisition Regulations System*

Therefore, 48 CFR parts 204, 232, and 252 are proposed to be amended as follows:

1. The authority citation for 48 CFR parts 204, 232, and 252 continues to read as follows:

**Authority:** 41 U.S.C. 1303 and 48 CFR chapter 1.

PART 204—ADMINISTRATIVE MATTERS

2. Amend section 204.1202 by—

- a. Revising the section heading;
- b. Redesignating paragraph (2)(xiii) as (2)(xiv); and
- c. Adding a new paragraph (2)(xiii)

The revision and addition read as follows:

**204.1202 Solicitation provision and contract clause.**

\* \* \* \* \*

(2) \* \* \*

(xiii) 252.232-70XX, Performance-Based Payments-  
Representation.

\* \* \* \* \*

**PART 232-CONTRACT FINANCING**

3. In section 232.1001, revise paragraph (a) to read as follows:

**232.1001 Policy.**

(a) In accordance with 10 U.S.C. 2307(b)(2), performance-based payments shall not be conditioned upon costs incurred in contract performance, but on the achievement of performance outcomes. Private sector companies, including nontraditional defense contractors, are eligible for performance-based payments, consistent with best commercial practices.

\* \* \* \* \*

4. Revise section 232.1003-70 to read as follows:

**232.1003-70 Criteria for use.**

In accordance with 10 U.S.C. 2307(b), the output of a contractor's accounting system shall be in compliance with Generally Accepted Accounting Principles, as evidenced by audited financial statements, in order to receive performance-

based payments. 10 U.S.C. 2307 does not grant the Defense Contract Audit Agency the authority to audit compliance with Generally Accepted Accounting Principles.

5. Amend section 232.1005-70 by—

- a. Designating the introductory text as paragraph (a);
- b. Redesignating paragraphs (a) and (b) as paragraphs (a) (1) and (2), respectively; and
- c. Adding a new paragraph (b).

The addition reads as follows:

**232.1003-70 Criteria for use.**

\* \* \* \* \*

(b) Use the provision at 252.232-70XX, Performance-Based Payments—Representation, in solicitations where the resulting contract may include performance-based payments.

**PART 252—SOLICITATION PROVISIONS AND CONTRACT CLAUSES**

6. Amend section 252.204-7007 by—

- a. Removing the provision date of “(APR 2018)” and adding “(DATE)” in its place; and
- b. Adding paragraph (d) (2) (vi) to read as follows:

**252.204-7007 Alternate A, Annual Representations and Certifications.**

\* \* \* \* \*

(d) \* \* \*

(2) \* \* \*



\_\_\_\_\_(vi) 252.232-70XX, Performance-Based Payments-Representation.

\* \* \* \* \*

7. Amend section 252.232-7012 by-

- a. In the clause introductory text, removing "232.1005-70(a)" and adding "232.1005-70(a)(1)" in its place;
- b. Removing the clause date of "(MAR 2014)" and adding "(DATE)" in its place;
- c. Redesignating paragraphs (b)(i) through (iii) as (c)(1) through (3), respectively;
- d. Adding a new paragraph (b); and
- e. Revising paragraph (c)(1).

The addition and revision reads as follows:

**252.232-7012 Performance-Based Payments-Whole-Contract Basis.**

\* \* \* \* \*

(b) In accordance with 10 U.S.C. 2307(b), the output of the Contractor's accounting system shall be in compliance with Generally Accepted Accounting Principles, as evidenced by audited financial statements, in order to receive performance-based payments.

(c)(1) The Contractor shall, in addition to providing the information required by FAR 52.232-32, submit supporting information for all payment requests using the following format:

Current performance-based payment(s) event(s) addressed by this request:		
Contractor shall identify—	Amount	Totals
(1a) Negotiated value of all previously completed performance-based payment(s) event(s);		
(1b) Negotiated value of the current performance-based payment(s) event(s);		
(1c) Cumulative negotiated value of performance-based payment(s) events completed to date (1a) + (1b); and		
(2) Total costs incurred to date.		

\* \* \* \* \*

8. Amend section 252.232-7013 by—

a. In the clause introductory text, removing “232.1005-70 (b)” and adding “232.1005-70 (a) (2)” in its place;

b. Removing the clause date of (APR 2014)” and adding “(DATE)” in its place;

c. Redesignating paragraphs (b) (i) through (iii) as (c) (1) through (3), respectively;

d. Adding a new paragraph (b); and

e. Revising newly redesignated paragraph (c) (1) .

The addition and revision read as follows:

**252.232-7013 Performance-Based Payments-Deliverable-Item Basis.**

\* \* \* \* \*

(b) In accordance with 10 U.S.C. 2307(b), the output of the Contractor's accounting system shall be in compliance with Generally Accepted Accounting Principles, as evidenced by audited financial statements, in order to receive performance-based payments.

(c) (1) The Contractor shall, in addition to providing the information required by FAR 52.232-32, submit supporting information for all payment requests using the following format:

Current performance-based payment(s) event(s) addressed by this request:		
Contractor shall identify-	Amount	Totals
(1a) Negotiated value of all previously completed performance-based payment(s) event(s);		
(1b) Negotiated value of the current performance-based payment(s) event(s);		
(1c) Cumulative negotiated value of		

performance-based payment(s) event(s) completed to date (1a) + (1b); and		
(2) Total costs incurred to date.		

\* \* \* \* \*

9. Add section 252.232-70XX to read as follows:

**252.232-70XX Performance-Based Payments-Representation**

As prescribed in 232.1005-70(b), use the following provision:

**PERFORMANCE-BASED PAYMENTS-REPRESENTATION (DATE)**

(a) In accordance with 10 U.S.C. 2307(b), the output of a contractor's accounting system shall be in compliance with Generally Accepted Accounting Principles in order to receive performance-based payments.

(b) The Offeror represents that the output of its accounting system is [ ] is not [ ] in compliance with Generally Accepted Accounting Principles, as evidenced by audited financial statements.

(End of Provision)

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